(*1*) Expenses for medical care described in section 213(d) previously incurred by the employee, the employee's spouse, or any dependents of the employee (as defined in section 152) or necessary for these persons to obtain medical care described in section 213(d);

(*2*) Costs directly related to the purchase of a principal residence for the employee (excluding mortgage payments);

(*3*) Payment of tuition, related educational fees, and room and board expenses, for the next 12 months of postsecondary education for the employee, or the employee's spouse, children, or dependents (as defined in section 152); or

(*4*) Payments necessary to prevent the eviction of the employee from the employee's principal residence or foreclosure on the mortgage on that residence.

(B) *Distribution deemed necessary to satisfy financial need.* A distribution is deemed necessary to satisfy an immediate and heavy financial need of an employee if all of the following requirements are satisfied:

(*1*) The distribution is not in excess of the amount of the immediate and heavy financial need of the employee. The amount of an immediate and heavy financial need may include any amounts necessary to pay any federal, state, or local income taxes or penalties reasonably anticipated to result from the distribution.

(*2*) The employee has obtained all distributions, other than hardship distributions, and all nontaxable (at the time of the loan) loans currently available under all plans maintained by the employer.

(*3*) The plan and all other plans maintained by the employer limit the employee's elective contributions for the next taxable year to the applicable limit under section 402(g) for that year minus the employee's elective contributions for the year of the hardship distribution.

(*4*) The employee is prohibited, under the terms of the plan or an otherwise legally enforceable agreement, from making elective contributions and employee contributions to the plan and all other plans maintained by the employer for at least 12 months after receipt of the hardship distribution. For this purpose the phrase ''all other plans maintained by the employer'' means all qualified and nonqualified plans of deferred compensation maintained by the employer. The phrase includes a stock option, stock purchase, or similar plan, or a cash or deferred arrangement that is part of a cafeteria plan within the meaning of section 125. However, it does not include the mandatory employee contribution portion of a defined benefit plan. It also does not include a health or welfare benefit plan, including one that is part of a cafeteria plan within the meaning of section 125. See §1.401(k)–1(g)(4)(i) for the continued treatment of suspended employees as eligible employees.

(C) *Commissioner may expand standards.* The Commissioner may expand the list of deemed immediate and heavy financial needs and may prescribe additional methods for distributions to be deemed necessary to satisfy an immediate and heavy financial need only in revenue rulings, notices, and other documents of general applicability, and not on an individual basis.

(3) *Rules applicable to distributions upon plan termination.* A distribution may not be made under paragraph (d)(1)(iii) of this section if the employer establishes or maintains a successor plan. For purposes of this rule, the definition of the term ''employer'' contained in paragraph (g)(6) of this section is applied as of the date of plan termination, and a successor plan is any other defined contribution plan maintained by the same employer. However, if at all times during the 24-month period beginning 12 months before the termination, fewer than two percent of the employees who were eligible under the defined contribution plan that includes the cash or deferred arrangement as of the date of plan termination are eligible under the other defined contribution plan, the other plan is not a successor plan. The term ''defined contribution plan'' means a plan that is a defined contribution plan as defined in section 414(i), but does not include an employee stock ownership plan as defined in section 4975(e) or 409(a) or a simplified employee pension as defined in section 408(k). A plan is a

successor plan only if it exists at any time during the period beginning on the date of plan termination and ending 12 months after distribution of all assets from the terminated plan.

(4) *Rules applicable to distributions upon sale of assets or subsidiary*—(i) *Seller must maintain the plan.* A distribution may be made under section 401(k)(10) and paragraph (d)(1) (iv) or (v) of this section only from a plan that the seller continues to maintain after the disposition. This requirement is satisfied if and only if the purchaser does not maintain the plan after the disposition. A purchaser maintains the plan of the seller if it adopts the plan or otherwise becomes an employer whose employees accrue benefits under the plan. A purchaser also maintains the plan if the plan is merged or consolidated with, or any assets or liabilities are transferred from the plan to a plan maintained by the purchaser in a transaction subject to section 414(*l*)(1). A purchaser is not treated as maintaining the plan merely because a plan that it maintains accepts elective transfers described in §1.411(d)–4, Q&A–3(b)(1), or rollover contributions of amounts distributed by the plan (including distributions that the recipient elects, under section 401(a)(31), to have paid in a direct rollover to the plan of the purchaser).

(ii) *Employee must continue employment.* A distribution may be made under paragraph (d)(1) (iv) or (v) of this section only to an employee who continues employment with the purchaser of assets or with the subsidiary, whichever is applicable.

(iii) *Distribution must be in connection with disposition of assets or subsidiary.* Elective contributions may not be distributed under paragraph (d)(1) (iv) or (v) of this section except in connection with the disposition that results in the employee's transfer to the purchaser. Whether a distribution is made in connection with the disposition of assets or a subsidiary depends on all of the facts and circumstances. Except in unusual circumstances, however, a distribution will not be treated as having been made in connection with a disposition unless it was made by the end of the second calendar year after the calendar year in which the disposition occurred.

(iv) *Definitions*—(A) *Substantially all.* For purposes of paragraph (d)(1)(iv) of this section, the sale of ''substantially all'' the assets used in a trade or business means the sale of at least 85 percent of the assets.

(B) *Unrelated employer.* For purposes of paragraph (d)(1) (iv) and (v) of this section, an ''unrelated'' entity or individual is one that is not required to be aggregated with the seller under section 414 (b), (c), (m), or (o) after the sale or other disposition.

(5) *Lump sum requirement for certain distributions.* After March 31, 1988, a distribution may be made under paragraph (d)(1) (iii), (iv), or (v) of this section only if it is a lump sum distribution. The term *lump sum distribution* has the meaning provided in section 402(d)(4), without regard to subparagraphs (A) (i) through (iv), (B), and (F) of that section.

(6) *Rules applicable to all distributions*—(i) *Impermissible distributions.* Amounts attributable to elective contributions may not be distributed on account of any event not described in this paragraph (d), such as completion of a stated period of plan participation or the lapse of a fixed number of years. For example, if excess deferrals (and income) for an employee's taxable year are not distributed within the time prescribed in §1.402(g)–1(e) (2) or (3), the amounts may be distributed only on account of an event described in this paragraph (d).

(ii) *Deemed distributions.* The cost of life insurance (P.S. 58 costs) is not treated as a distribution for purposes of section 401(k)(2) and this paragraph. The making of a loan is not treated as a distribution, even if the loan is secured by the employee's accrued benefit attributable to elective contributions or is includible in the employee's income under section 72(p). However, the reduction, by reason of default on a loan, of an employee's accrued benefit derived from elective contributions is treated as a distribution.

(iii) *ESOP dividend distributions.* A plan does not fail to satisfy the requirements of this paragraph (d) merely by reason of a dividend distribution described in section 404(k)(2).

(iv) *Limitations apply after transfer.* The limitations of this paraqraph (d) generally continue to apply to amounts attributable to elective contributions (including amounts treated as elective contributions) that are transferred to another qualified plan of the same or another employer. Thus, the transferee plan will generally fail to satisfy the requirements of section 401(a) and this section if transferred amounts may be distributed before the times specified in this paragraph (d). The limitations of paragraph (d) of this section cease to apply after the transfer, however, if the amounts could have been distributed at the time of the transfer (other than on account of hardship), and the transfer is an elective transfer described in §1.411(d)–4, Q&A–3(b)(1). The limitations of paragraph (d) of this section also do not apply to amounts distributed from another plan that the recipient elects under section 401(a)(31) to have paid in a direct rollover to the plan.

(v) *Required consent.* A distribution may be made under this paragraph (d) only if any consent or election required under section 411(a)(11) or 417 is obtained.

(7) *Examples.* The provisions of this paragraph (d) are illustrated by the following examples:

Example 1. Employer C maintains a profit-sharing plan that includes a cash or deferred arrangement. Elective contributions under the arrangement may be withdrawn for any reason after two years following the end of the plan year in which the contributions were made. Because the plan permits distributions of elective contributions before the occurrence of one of the events specified in section 401(k)(2)(B) and this paragraph (d), the plan includes a nonqualified cash or deferred arrangement and the elective contributions are currently includible in income under section 402.

Example 2. Employer D maintains a pre-ERISA money purchase plan that includes a cash or deferred arrangement. Elective contributions under the arrangement may be distributed to an employee on account of hardship. Under paragraph (d)(1) of this section, hardship is a distribution event only in a profit-sharing or stock bonus plan. Since elective contributions under the arrangement may be distributed before a distribution event occurs, the cash or deferred arrangement does not satisfy this paragraph (d), and is not a qualified cash or deferred arrangement. Moreover, the plan is not a qualified plan because a pension plan may not provide for payment of benefits upon hardship. See §1.401–1(b)(1)(i).

(e) *Additional requirements for qualified cash or deferred arrangements*—(1) *Qualified profit-sharing, stock bonus, pre-ERISA money purchase or rural cooperative plan requirement.* A cash or deferred arrangement satisfies this paragraph (e) only if the plan of which it is a part is a profit-sharing, stock bonus, pre-ERISA money purchase or rural cooperative plan that otherwise satisfies the requirements of section 401(a) (taking into account the cash or deferred arrangement). A plan that includes a cash or deferred arrangement may provide for other contributions, including employer contributions (other than elective contributions), employee contributions, or both. See paragraph (e)(7) of this section, however, for limitations on the extent to which elective contributions under a cash or deferred arrangement may be taken into account in determining whether the other contributions satisfy the requirements of section 401(a).

(2) *Cash availability requirement.* A cash or deferred arrangement satisfies this paragraph (e) only if the arrangement provides that the amount that each eligible employee may defer as an elective contribution is available to the employee in cash. Thus, for example, if an eligible employee is provided the option to receive a taxable benefit (other than cash) or to have the employer contribute on the employee's behalf to a profit-sharing plan an amount equal to the value of the taxable benefit, the arrangement is not a qualified cash or deferred arrangement. Similarly, if an employee has the option to receive a specified amount in cash or to have the employer contribute an amount in excess of the specified cash amount to a profit-sharing plan on the employee's behalf, any contribution made by the employer on the employee's behalf in excess of the specified cash amount is not treated as made pursuant to a qualified cash or deferred arrangement. This cash availability requirement applies even if the cash or deferred arrangement is part of a cafeteria plan within the meaning of section 125.

(3) *Separate accounting requirement*—(i) *General rule.* A cash or deferred arrangement satisfies this paragraph (e) only if the portion of an employee's benefit subject to the requirements of paragraphs (c) and (d) of this section is determined by an acceptable separate accounting between that portion and any other benefits. Separate accounting is not acceptable unless gains, losses, withdrawals, and other credits or charges are separately allocated on a reasonable and consistent basis to the accounts subject to the requirements of paragraphs (c) and (d) of this section and to other accounts. Subject to section 401(a)(4), forfeitures are not required to be allocated to the accounts in which benefits are subject to paragraphs (c) and (d) of this section.

(ii) *Failure to satisfy separate accounting requirement.* The requirements of paragraph (e)(3)(i) of this section are treated as satisfied if all amounts held under a plan that includes a cash or deferred arrangement or under another plan, contributions under which are taken into account under the arrangement for purposes of paragraph (b) of this section are treated as attributable to elective contributions subject to the requirements of paragraphs (c) and (d) of this section.

(4) *Limitations on cash or deferred arrangements of state and local governments and tax-exempt organizations*—(i) A cash or deferred arrangement does not satisfy the requirements of this paragraph (e) if the arrangement is adopted:

(A) After May 6, 1986, by a state or local government or political subdivision thereof, or any agency or instrumentality thereof (''a governmental unit''), or

(B) After July 1, 1986, by any organization exempt from tax under subtitle A of the Internal Revenue Code.

For purposes of paragraph (e)(4) of this section, whether an organization is exempt from tax under subtitle A of the Internal Revenue Code is determined without regard to section 414 (b), (c), (m) or (o).

(ii) A cash or deferred arrangement is treated as adopted after the dates described in paragraph (e)(4)(i) of this section with respect to all employees of any employer that adopts the arrangement after such dates. If an employer adopted an arrangement prior to such dates, all employees of the employer may participate in the arrangement.

(iii) For purposes of this paragraph (e)(4), an employer that has made a legally binding commitment to adopt a cash or deferred arrangement is treated as having adopted the arrangement on that date.

(iv) If a governmental unit adopted a cash or deferred arrangement before May 7, 1986, then any cash or deferred arrangement adopted by the unit at any time is treated as adopted before that date.

(v) This paragraph (e)(4) does not apply to a rural cooperative plan.

(vi) For purposes of this paragraph (e)(4), an employee representative is treated as an employee of a tax exempt employer even if the employee could be treated as an employee by another employer under § 1.413–1(i)(1).

(5) *One-year eligibility requirement.* For plan years beginning after December 31, 1988, or such later date provided in paragraph (h) of this section, a cash or deferred arrangement satisfies this paragraph (e) only if no employee is required to complete a period of service greater than one year (determined without regard to section 410(a)(1)(B)(i)) with the employer maintaining the plan to be eligible to make an election under the arrangement.

(6) *Other benefits not contingent upon elective contributions*—(i) *General rule.* For plan years beginning after December 31, 1988, or such later date provided in paragraph (h) of this section, a cash or deferred arrangement satisfies this paragraph (e) only if no other benefit is conditioned (directly or indirectly) upon the employee's electing to make or not to make elective contributions under the arrangement. The preceding sentence does not apply to any matching contribution (as defined in section 401(m)) made by reason of such an election or to any benefit that is provided at the employee's election under a plan described in section 125(d) in lieu of an elective contribution under a qualified cash or deferred arrangement.

(ii) *Definition of other benefits.* Other benefits include, but are not limited to, benefits under a defined benefit plan; nonelective employer contributions under a defined contribution plan; the

availability, cost, or amount of health benefits; vacations or vacation pay; life insurance; dental plans; legal services plans; loans (including plan loans); financial planning services; subsidized retirement benefits; stock options; property subject to section 83; and dependent care assistance. Also, increases in salary and bonuses (other than those actually subject to the cash or deferred election) are benefits for purposes of this paragraph (e)(6). The ability to make after-tax employee contributions is a benefit, but that benefit is not contingent upon an employee's electing to make or not make elective contributions under the arrangement merely because the amount of elective contributions reduces dollar-for-dollar the amount of after-tax employee contributions that may be made. Benefits under any other plan or arrangement (whether or not qualified) are not contingent upon an employee's electing to make or not to make elective contributions under a cash or deferred arrangement merely because the elective contributions are or are not taken into account as compensation under the other plan or arrangement for purposes of determining benefits.

(iii) *Effect of certain statutory limits.* A benefit under a defined benefit plan that is contingent upon elective contributions solely by reason of the combined plan fraction of section 415(e) is not treated as contingent for purposes of this paragraph (e)(6). Similarly, any benefit under an excess benefit plan described in section 3(36) of the Employee Retirement Income Security Act of 1974 that is dependent on the employee's electing to make or not to make elective contributions is not treated as contingent.

(iv) *Nonqualified deferred compensation.* Participation in a nonqualified deferred compensation plan is treated as contingent for purposes of this paragraph (e)(6) only to the extent that an employee may receive additional deferred compensation under the nonqualified plan to the extent the employee makes or does not make elective contributions. Deferred compensation under a nonqualified plan of deferred compensation that is dependent on an employee's having made the maximum elective deferrals under section 402(g) or the maximum elective contributions permitted under the terms of the plan also is not treated as contingent.

(v) *Plan loans and distributions.* A loan or distribution of elective contributions is not a benefit conditioned on an employee's electing to make or not make elective contributions under the arrangement merely because the amount of the loan or distribution is based on the amount of the employee's account balance.

(vi) *Examples.* The provisions of this paragraph (e)(6) are illustrated by the following examples.

Example 1. Employer T maintains a cash or deferred arrangement for all of its employees. Employer T also maintains a nonqualified deferred compensation plan for two highly paid executives, Employees R and C. Under the terms of the nonqualified deferred compensation plan, R and C are eligible to participate only if they do not make elective contributions under the cash or deferred arrangement. Participation in the nonqualified plan is a contingent benefit for purposes of this paragraph (e)(6), because R's and C's participation is conditioned on their electing not to make elective contributions under the cash or deferred arrangement.

Example 2. Employer T maintains a cash or deferred arrangement for all its employees. Employer T also maintains a nonqualified deferred compensation plan for two highly paid executives, Employees R and C. Under the terms of the arrangements, Employees R and C may defer a maximum of 10 percent of their compensation, and may allocate their deferral between the cash or deferred arrangement and the nonqualified deferred compensation plan in any way they choose (subject to the overall 10 percent maximum). Because the maximum deferral available under the nonqualified deferred compensation plan depends on the elective deferrals made under the cash or deferred arrangement, the right to participate in the nonqualified plan is a contingent benefit for purposes of paragraph (e)(6).

(7) *Coordination with other plans.* For plan years beginning after December 31, 1988, or such later date provided in paragraph (h) of this section, a cash or deferred arrangement satisfies this paragraph (e) only if no elective contributions (or qualified matching contributions treated as elective contributions under paragraph (b)(5) of this section) under the arrangement are taken into account for purposes of determining whether any other contributions

under any plan (including the plan to which the elective contributions are made) satisfy the requirements of section 401(a). Indeed, the portion of a plan that consists of elective contributions is treated as a separate plan for purposes of sections 401(a)(4) and 410(b). See §1.410(b)–7(c)(1). Similarly, elective contributions under a cash or deferred arrangement generally may not be taken into account in determining whether a plan satisfies the minimum contribution or benefit requirements of section 416. See §1.416–1, M–20. However, qualified nonelective contributions that are treated as elective contributions for purposes of section 401(k)(3) under paragraph (b)(5) of this section may be used to enable a plan to satisfy the minimum contribution or benefit requirements under section 416. See §1.416–1, M–18. This paragraph (e) does not apply for purposes of determining whether a plan satisfies the average benefit percentage requirement of section 410(b)(2)(A)(ii). See also §1.401(m)–1(b)(5) for circumstances under which elective contributions may be used to determine whether a plan satisfies the requirements of section 401(m).

(8) *Recordkeeping requirements.* For plan years beginning after December 31, 1986, or such later date provided in paragraph (h) of this section, a cash or deferred arrangement satisfies this paragraph (e) only if the employer maintains the records necessary to demonstrate compliance with the applicable nondiscrimination requirements of paragraph (b) of this section, including the extent to which qualified nonelective contributions and qualified matching contributions are taken into account.

(9) *Consistent application of separate line of business rules.* If an employer is treated as operating qualified separate lines of business under section 414(r) in accordance with §1.414(r)–1(b) for purposes of applying section 410(b), and applies the special rule for employer-wide plans in §1.414(r)–1(c)(2)(ii) to the portion of the plan that consists of contributions under the cash or deferred arrangement, then the requirements of section 401(k) and this section must be applied on an employer-wide rather than a qualified-separate-line-of-business basis to all of the plans or portions of plans taken into account in determining whether the cash or deferred arrangement is a qualified cash or deferred arrangement, regardless of whether those plans or portions of plans also satisfy the requirements necessary to apply the special rule in §1.414(r)–1(c)(2)(ii). Conversely, if an employer is treated as operating qualified separate lines of business under section 414(r) in accordance with §1.414(r)–1(b) for purposes of applying section 410(b), and does not apply the special rule for employer-wide plans in §1.414(r)–1(c)(2)(ii) to the portion of the plan that consists of contributions under the cash or deferred arrangement, then the requirements of section 401(k) and this section must be applied on a qualified-separate-line-of-business rather than an employer-wide basis to all of the plans or portions of plans taken into account in determining whether the cash or deferred arrangement is a qualified cash or deferred arrangement, regardless of whether one or more of those plans or portions of plans is tested under the special rule §1.414(r)–1(c)(2)(ii). This requirement applies solely for purposes of determining whether the cash or deferred arrangement is a qualified cash or deferred arrangement under section 401(k) and this section. The rules of this paragraph are illustrated by the following example.

Example. (i) Employer A maintains a profit-sharing plan that includes a cash or deferred arrangement in which all of the employees of Employer A are eligible to participate. Employer A is treated as operating qualified separate lines of business under section 414(r) in accordance with §1.414(r)–1(b) for purposes of applying section 410(b). However, Employer A applies the special rule for employer-wide plans in §1.414(r)–1(c)(2)(ii) to the portion of its profit-sharing plan that consists of elective contributions under the cash or deferred arrangement (and to no other plans or portions of plans). Employer A makes qualified nonelective contributions to the profit-sharing plan for the 1995 plan year, and the profit-sharing plan provides that these qualified nonelective contributions may be used to satisfy the actual deferral percentage test.

(ii) Under these facts, the requirements of sections 401(a)(4) and 410(b) must be applied on an employer-wide rather than a qualified-